



global witness

SOUTH SUDAN

THE CALL FOR A MORATORIUM ON NEW OIL CONTRACTS



Photo courtesy of Jared Ferris, Reuters

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South Sudan is in the midst of a violent crisis, and is experiencing widespread instability. The country's oil resources have become a central focus of the violence, and revenues from the sector have been diverted away from development and towards military spending. The conflict has fragmented systems of authority and undermined democratic structures, heightening the risk of corruption, and creating an extremely unstable investment environment, which is likely to dissuade the most responsible companies and the most favourable deals. South Sudan's oil legislation, which is designed to prevent corruption and ensure that deals are beneficial to the country in the long run, is not yet in place, meaning that negotiations at this time risk not being subject to strong regulation and review. In light of these circumstances, Global Witness is calling on the government of South Sudan to issue a moratorium on all new oil sector contracts and to call a halt to all contract renegotiations, until peace and the rule of law are restored.

WHY SHOULD SOUTH SUDAN SUSPEND NEW OIL DEALS?

High-risk deals could be signed on bad terms for South Sudanese citizens

Deals signed during times of crisis and in the absence of robust legal frameworks often secure less favourable terms for governments, meaning that in the long run, South Sudanese citizens could benefit less from the exploitation of their natural resources. In addition, increased instability can dissuade responsible investors with good track records and experience in the sector, putting communities and environments near oil-producing areas at greater risk of disruption and damage caused by less qualified companies.

The Mittal deal in post-conflict Liberia is an example of an extractive industry contract signed without a robust governance framework in place, which failed to secure favourable terms for the government. The 2003 Accra Peace Agreement installed the National Transitional Government of Liberia, bringing together former warring factions.



Women carry their belongings as they head for shelter in the United Nations Mission in South Sudan (UNMISS) base in Malakal, Upper Nile state, January 2014.

Photo courtesy of Mackenzie Knowles-Coursin, Associated Press.

The transitional government swiftly sold off access to the country's natural resources, including through a 2005 iron ore contract with Mittal Steel. The contract contained terms that were highly advantageous to the company, allowing Mittal to determine tax rates and giving the company control over some of Liberia's most important infrastructure, such as a major railway line and the port at Buchanan.

In October 2006, Global Witness drew attention to the Mittal case through a detailed analysis of the contract.¹ The following year the company agreed to a renegotiation with the new Liberian government, headed now by President Ellen Johnson Sirleaf. The revised contract has removed some of the most harmful provisions contained in the initial agreement.

New revenues are unlikely to be used for development

Revenues from South Sudan's oil sector should be invested in the much-needed development of infrastructure and social services that will benefit all citizens. There is a risk that while the country is in conflict, revenue from new projects – multi-million dollar signature bonuses for example – will be diverted to the defence budget. Limited government funds have already been redirected to fund the war: in February 2014 the Minister of Finance presented a supplementary budget of 750 million South Sudanese pounds to the National Legislature of which 500

million (around US\$160 million at current exchange rates) was earmarked for defence spending.² The oil sector is South Sudan's main source of cash for development and revenues diverted to finance the conflict can never be recovered.

Oil legislation remains stalled

South Sudan's much-lauded oil legislation is designed to prevent bad deals, corruption and irresponsible investors entering the sector. It is critical that this legislation is fully implemented before any new contracts are negotiated or signed. If comprehensively applied, it will ensure companies bidding for new exploration and production sharing agreements (EPSAs) are qualified, and that bidding processes are open and competitive.

The Petroleum Act 2012 requires that new contracts are made public, providing an opportunity for independent verification that the terms are in the best interests of the country, and making environmental and social safeguards meaningful

by allowing citizens to be fully informed of their rights.³ However, the Act has yet to be fully implemented and its partner legislation, the Petroleum Revenue Management Bill, is stalled awaiting signature in the President's office. Donor-funded technical experts embedded in the Ministry of Petroleum and Mining left the country when conflict broke out and have yet to return, further slowing implementation.

The Aynak deal in Afghanistan highlights how contracts signed without adequate transparency legislation in place are unlikely to be in the best long-term interests of citizens.⁴ It was signed with a Chinese-backed consortium in 2008 to mine the country's largest known copper concession at Mes Aynak in Logar province. The project had the potential to generate an estimated US\$541 million per year for the government, creating 5,000 jobs and bringing in much needed infrastructure investment. However, these benefits were seriously undermined by secrecy around the contract's terms. The contract included extremely favourable

CRITICAL CLAUSES FOR CONTRACTING IN THE PETROLEUM ACT 2012

Section 18, clause 2

"Petroleum agreements shall be entered into following an open, transparent, non-discriminatory and competitive tender process conducted in accordance with applicable law governing public procurement."

Section 18, clause 4

"Petroleum agreements may only be entered into with a company or group of companies with the requisite technical competence, sufficient experience, history of compliance and ethical conduct and financial capacity to adequately fulfil all obligations of the petroleum agreements, applicable law and any other requirements stipulated by the Ministry."

Section 79, clause 1

The Minister shall make available to the public, both on the ministry website and by any other appropriate means to inform interested persons:

(a) All key oil sector production, revenue and expenditure data, petroleum agreements and licenses and,

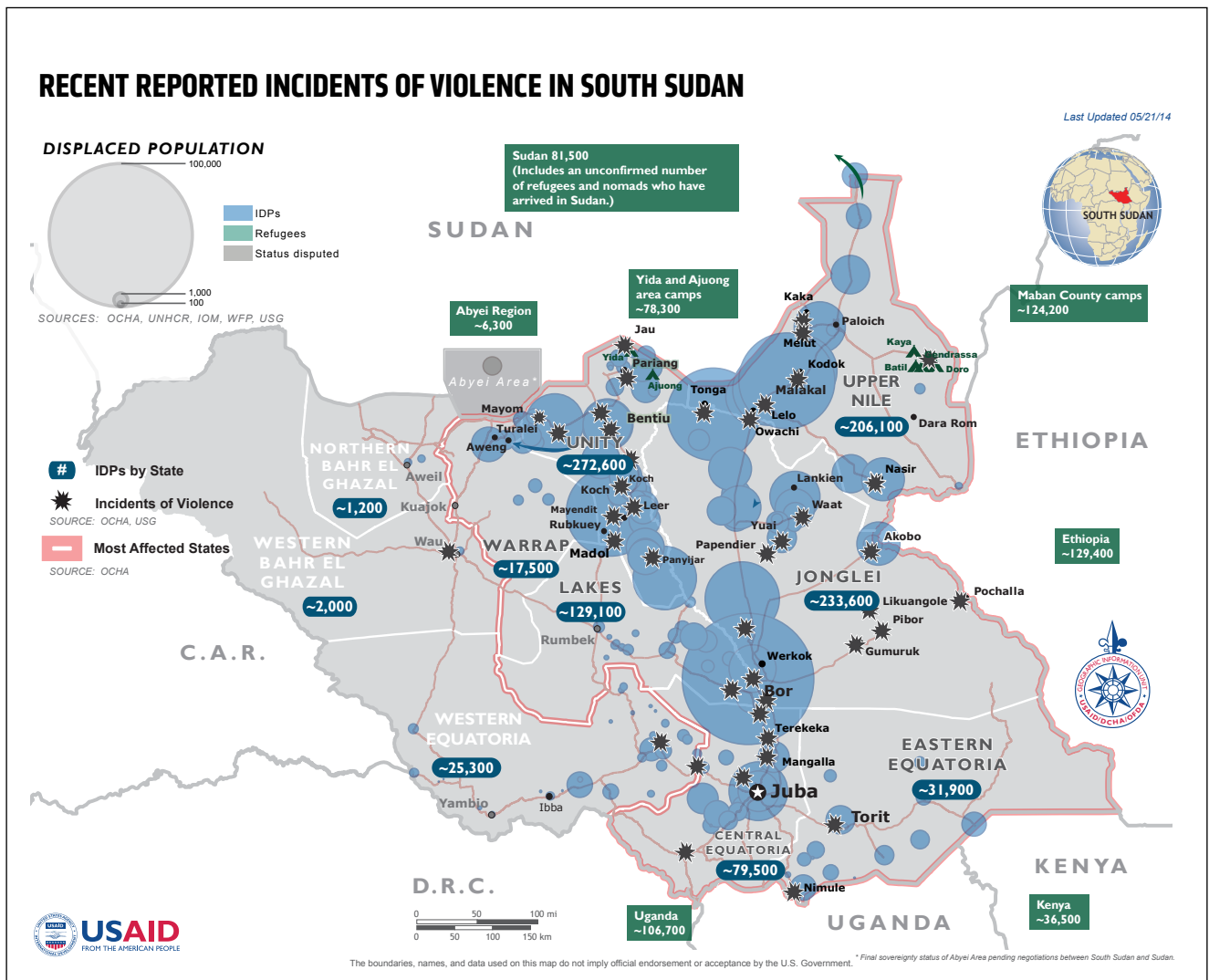
(c) justification of award of petroleum agreements, the beneficial ownership information for the contractor and documented proof of the requisite technical competence, sufficient experience, history of compliance and ethical conduct and financial capacity of the contractor.

economic terms for the company, including a mechanism to cut the royalty rates to match other natural resource contracts, and six months of exclusive rights to bid for other resources.

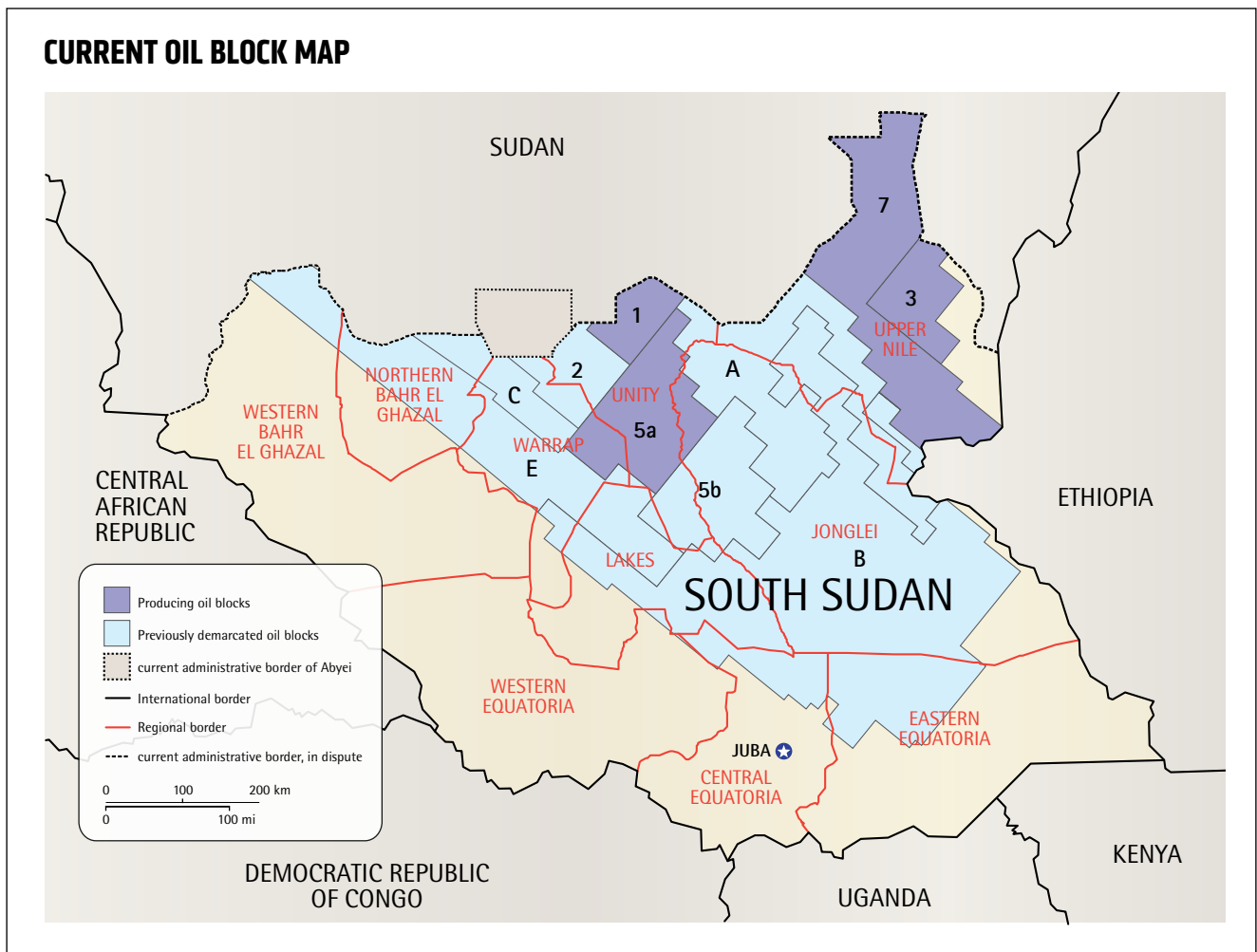
The Chinese company that won the contract has since asked to re-negotiate it in a way that would eliminate almost all of the elements which made their bid attractive in the first place.⁵ Without access to the original contract, Afghanistan's citizens cannot properly scrutinise and query either the original terms or discussions over changes. Furthermore, by not making the contract public, the government undermined social and environmental safeguards: without knowledge of their rights, and the compensation due if these rights were violated, affected communities were seriously disadvantaged when dealing with the consortium.

Influx of armed actors could exacerbate existing conflicts

The oil concessions Global Witness believes to be currently under negotiation – blocks B1, B2 and B3 – are located mainly in Jonglei and Lakes states, which pose significant security challenges. Jonglei has witnessed continued inter-ethnic conflict, and violence between government forces and local militias since independence.⁶ The state capital, Bor was one of the initial flashpoints when the current crisis began in December, and parts of the state are currently under rebel control. Lakes state has also witnessed sustained inter-communal violence since independence, and has seen large-scale displacement and violence during the recent conflict. If contracts for these concessions are granted, companies would need to employ armed security forces in order to operate. In a region already home to high numbers of military and militias, a further influx of armed actors could worsen or prolong conflict.



Violence has been concentrated in the oil producing states of Unity and Upper Nile, and in Jonglei state.



WHAT WOULD A MORATORIUM ON NEW OIL DEALS LOOK LIKE?

The government should comprehensively address the risks outlined above by:

- prohibiting the negotiation or signature of new exploration and production agreements (EPSAs);
- prohibiting the negotiation or signature of new midstream deals, refinery or transportation contracts;
- calling a halt to the renegotiation of EPSAs awarded before independence.
- peace and stability have been re-established across South Sudan;
- the Petroleum Act 2012 and the Petroleum Revenue Management Bill have been passed and comprehensively implemented;
- reports of human rights abuses by both sides, particularly in oil-producing areas, have been investigated and those found guilty held to account.

To be effective, a moratorium should remain in place until conditions are favourable for a stable, profitable oil sector, which benefits all of South Sudan's citizens, that is until:

WHERE ELSE HAVE MORATORIUMS SUCCESSFULLY MITIGATED CONFLICT OR CORRUPTION RISK?

Uganda's oil sector

After making commercially viable discoveries in 2006, the Ugandan government issued a moratorium on new licenses in 2007. At the time of the discoveries the government lacked the institutional capacity and knowledge of the potential finds to govern the sector effectively. Although developments in Uganda's oil industry are less advanced than in South Sudan where production is already underway, the country provides a useful comparison because the legal framework to govern the sector is at a similar preliminary stage.

Since the moratorium was issued in Uganda, new oil laws have been passed to govern the upstream and midstream sectors, officials have been trained in the Ministries of Energy, Environment and Finance, and a national oil company has been established. In addition, the government has had time to collect and assess data on the potential reserves.⁷ As a result, Uganda is now in a much improved position to allocate and enforce contracts on good financial terms for the government, to ensure that contracts include strong environmental and social safeguards, and to market the government's share of oil production.

South Sudan's mining sector

In November 2010, the southern Sudan Legislative Assembly issued a moratorium on mining licenses. The decision followed several years of administrative confusion in the sector after the 2005 Comprehensive Peace Agreement was signed, leading to licences being awarded with no assessment of the companies' expertise or background, and concessions being allocated to multiple companies simultaneously.⁸

The moratorium has allowed the government time to develop the Mining Act 2012, and to build capacity to monitor the activities of mining companies in the future.⁹ Concerns around community rights, revenue management and militarisation of the sector remain to be addressed before new licences are awarded. However, the moratorium allowed some space for the foundations of good governance to be laid.

Liberia's forestry sector

In 2012, Liberian President Ellen Johnson Sirleaf announced a moratorium on newly-issued 'Private Use Permits' (PUPs) for the forestry sector. Intended to allow private landowners to clear forest on their land, companies used PUPs to cut timber while avoiding the taxes and environmental standards applicable to other large logging contracts. Sixty three PUPs were issued in the space of two years using fraudulent documentation, giving logging companies the rights to clear 40% of Liberia's forests.¹⁰

The moratorium effectively halted any new private use permits being issued, pending an official investigation into the impact that the existing permits would have on communities and the environment. Ultimately, the investigation recommended that all the permits issued should be cancelled, preventing the illegal logging of one of Liberia's most precious resources.



ENDNOTES

- 1 Global Witness, 2006, "Heavy Mittal", accessed at <http://bit.ly/1mG9aN0>
- 2 Eye Radio, 2014, "Gov't sets aside 750 million pounds as emergency funds", <http://bit.ly/1pyD4n2>
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- 4 Global Witness, 2012, "Copper Bottomed? Bolstering the Aynak contract: Afghanistan's first major mining deal", accessed at <http://bit.ly/1hz2P1r>
- 5 South China Morning Post, 2014, "China's MCC turns back on US\$3b Mes Aynak Afghanistan mine deal" accessed at <http://bit.ly/1iw1AUG>
- 6 IRIN, 2012, "South Sudan: briefing on Jonglei violence", accessed at <http://bit.ly/1k6TGSm>
- 7 Government of Uganda Petroleum Exploration and Production Department, "The History and Progress of Petroleum Exploration and Development in Uganda", accessed at <http://bit.ly/1wqYNC6>
- 8 United States Institute of Peace, 2013, "Establishing a Mining Sector in Postwar South Sudan", accessed at <http://bit.ly/1pn3IY3>
- 9 The Mining Act 2012 accessed at <http://bit.ly/1isO1BL>
- 10 Global Witness, SDI, Save my Future Foundation, 2012, "Signing their Lives away: Liberia's Private Use Permits and the Destruction of Community-Owned Rainforest", accessed at <http://bit.ly/1tT8R4D>

FRONT COVER PHOTOGRAPH

Soldiers at an oil facility in Palouge, Upper Nile state, January 2012.

Global Witness is a UK based non-governmental organisation which investigates the role of natural resources in funding conflict and corruption around the world.

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